

Charity Asset Distribution on Dissolution: Who Decides?

07.13.17 | Linda J. Rosenthal, JD



When a 501(c)(3) charitable organization winds up its affairs, a key issue is the distribution of assets on the dissolution.

Under federal tax law, a 501(c)(3)'s organizing documents must specify that its assets will be “irrevocably dedicated to charitable purposes.”

The laws of most – if not all – U.S. states include a similar limitation.

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The critical task of the disposition of assets must meet the standards of the Internal Revenue Service Code and any applicable state laws. In general, a nonprofit's assets may not be distributed to a board of directors, staff, or other organizational insiders. Most states require that an organization's assets be distributed to other charitable organizations or governmental bodies. These laws ensure that assets amassed for charitable or other nonprofit activities continue to be used for similar purposes.

When that moment arrives, who decides which other group or groups will be given these valuable assets? Who decides, and how is it decided?

Two recent cases in New Hampshire are interesting examples.

City Challenges Charity Asset Plan

Nashua is the second-largest city in New Hampshire. Recently, a “mysterious arts nonprofit” there – the Nashua Center for the Arts – filed a dissolution petition. Founded in the 1960’s, it has nearly \$1 million in assets.

The lucky designee for these funds: the Currier Museum of Art in Manchester, New Hampshire – some 20 miles away.

But this transfer is not going off without a hitch: The City of Nashua wants the money to remain in Nashua, and has launched a legal challenge.

Under New Hampshire law, a charitable organization that dissolves must distribute its assets according to its articles of incorporation and bylaws. This group has a murky history, though. “Many were apparently unaware that the organization was still in operation in recent years.”

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Sometime in the 1990s, (Nashua Center for the Arts) dissolved after falling on financial hard times. It was dormant for a while, then in 2003, when the Nashua Charitable Trust merged with the New Hampshire Charitable Trust, there was this money left over from the will of a woman named Edith Carter. She had given about \$200,000 to the Nashua Charitable Trust to promote arts in the city. So it was decided to revive the Nashua Center for the Arts so it could manage this money. Today, that money is over \$900,000, and [... it’s unclear...] ... exactly what they’ve [been] doing with it.

According to the past 3 years’ Form 990s, the group has awarded less than \$20,000 to only five organizations – all in Nashua including – for example – Nashua Sculpture Symposium and Symphony NH (Nashua).

“[T]he Nashua Center for the Arts’ broad mission [is] to promote arts in the region.” Its five current trustees are reportedly not explaining that in an any more meaningful way.

The attorney general of Nashua has asked the local probate court to order that the money be given to “arts nonprofits that focus on the city.” They could certainly “use the funding, particularly at a time when the National Endowment for the Arts is endangered.” The city has wanted to build a \$20 million performing arts center, but that plan has not yet moved beyond the feasibility-study phase. The Currier Museum of Art “primarily focuses on operation of its museum in Manchester,” but it also serves young children with arts enrichment at a Nashua HeadStart program.

So, how will the case be decided? “What does the Nashua Center for the Arts owe its donors and its home?” asks a columnist for the Nonprofit Quarterly, who suggests that the organization didn’t follow nonprofit expert Lee Bruder’s golden rules, including, “A successful dissolution preserves an organization’s legacy and contributes to a positive collective memory of the organization.”

Who Gets a Failing College’s Endowment?

“While very few of the higher education institutions closing each year [in the U.S.] are private nonprofit schools, the annual number has tripled since the recession and is anticipated to remain stable or increase further, according to a 2015 Moody’s report. Many of the schools most at risk have fewer than 500 students and are affiliated with religious denominations.”

When a college or university goes bankrupt, what happens to its endowment? Many have little or no money left, but when there are funds left, “there can be a fight between creditors, or between successor institutions taking up the responsibility of educating students.”

That’s what happened when New Hampshire’s Chester College closed down. The designated recipient was New England College, an institution that comes within the standard practice of nonprofits giving assets “to other nonprofits with similar missions, services, clientele, etc.”

There was a twist, though: the New England Institute of Art challenged the transfer, arguing that since it would be taking some 92% of Chester College’s students, the endowment should follow to it.

Here, we don’t have to wait for the judge’s ruling. The funds were split 60/40 between the two schools; the originally designated recipient, New England College, received the larger amount.

Conclusion

“In most cases of nonprofit dissolution, executives and board members learn that the state attorney general is the nonprofit’s ultimate arbiter and trustee. The AG must sign off on asset distribution and has standing to challenge any distribution that, in the AG’s opinion, harms the state’s citizens or denies them appropriate access to assets intended for a public purpose.”